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KEYNES, kanz, John Maynard (1883-1946)

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KEYNES, kānz, John Maynard (1883-1946), English economist, whose work was influential in ending "laissez faire" as the dominant rule for economic policy. Although a variant of economic theory is called Keynesian economics, Keynes did not found a school; he set off a series of movements that radically changed the ways economists view the world and the perceptions of economists and the public about the possibility of controlling the economy.

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Life. Keynes was born in Cambridge, England, on July 5, 1883. His father, John Neville Keynes, was a university lecturer and outstanding administrator at Cambridge University and the author of a standard book on The Scope and Methods of Political Economy.

Keynes was educated at Eton (1897-1902) and Cambridge (Kings College) (1902-05). He studied economics for a civil service examination and worked in the India Office (1906-08). He became a lecturer in economics at Cambridge (1908), fellow of King's College (1909), editor of the Economic Journal, and secretary of the Royal Economic Society (1911). In 1915 he accepted a position in the British treasury.

He was the principal representative of the treasury at the Paris Peace Conference (1919). Emotionally disturbed by developments at the conference, he resigned and wrote The Economic Consequences of the Peace (1919), in which he strongly objected to the economic-reparations features of the Treaty of Versailles.

After World War I, Keynes worked in London during the week~~, while~~ teaching and carry~~ing~~ out supervisory duties at Cambridge on weekends. Between 1920 and World War II his principal publications were A Treatise on Probability (1921), A Tract on Monetary Reform (1923), A Treatise on Money (1925), Essays in Persuasion (1931), Essays in Biography (1933), and The General Theory of Employment, Interest and Money (1936). In 1937, Keynes contracted a heart ailment that essentially ended his career as an academic economist.

In 1940, Keynes became an adviser to the chancellor of the exchequer. He was a principal British delegate and negotiator at the Bretton Woods Conference (1944), Stage II of Lend Lease (1944), arrangements for a United States loan to Britain (1945), and the inauguration of the International Monetary Fund and the International Bank (1946). Keynes was a main architect of the structure of international monetary and financial institutions that arose after World War II. In 1942 he was named 1st Baron Keynes of Tilton.

In 1925, Keynes married Lydia Lopakova, who had come to England with Diaghilev's Ballet. Throughout his adult life he maintained a close friendship with a group of brilliant authors, artists, and philosophers. Later, with additions, they constituted the Bloomsbury group. He died on April 21, 1946, in Firle, Sussex.

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Works. Keynes' main fame as an economist rests upon The General Theory of Employment, Interest and Money (1936). In this work Keynes took issue with the ruling economic theory of his day, the neoclassical theory of Alfred Marshall, and the proposition that asserted that the normal functioning of a market (capitalist) economy leads to full employment. Keynes showed that a market economy can operate at less than full employment and that market processes can be ineffective and even perverse in eliminating unemployment. His analysis of how monetary and financial arrangements affect the economy is the rock upon which arguments for active governmental fiscal and monetary policies rest. Keynes' revolution transformed economics from a descriptive and analytic study into a policy-oriented discipline that is relevant for the management of a capitalist economy. To Keynes, enlightened intervention by the government in the economy would show better results than those achieved by policies of laissez faire.

Keynes' General Theory is an inquiry into the principles that determine the overall behavior of a capitalist economy. This work, together with Keynes' contributions to the interpretative literature that followed its publication, was the culmination of Keynes' career as an economist. It dealt with the interrelations among the monetary, financial, exchange, and production dimensions of an economy that is explicitly capitalist, in the sense that businessmen and bankers interact to finance investment activity.

The analytic method of standard economic theory (both pre-Keynesian and today's) is first to analyze exchange and production, while abstracting from monetary matters, and then to modify the results in the light of monetary considerations. This methodology leads to the quantity theory of money and to propositions that exchange and production determine relative prices and money determines the "price level" (in the modern quantity theory money determines money income).

In The General Theory, Keynes broke with this tradition. He integrated money and finance into the determination of both output and relative prices. He did this by making investment depend upon financial and monetary factors and by having the markup on labor costs in the various productions depend in "equilibrium" on the ratio of output to the cost of capital assets. Whereas standard economics takes exchange to be the basic activity, Keynes viewed investment and its financing as the economic activity that characterizes a capitalist economy.

Owning and operating capital assets together with investing involve time: capital assets provide inputs to production processes over time, and financial instruments are promises to make payments over time. Because time is involved, decisions to invest, finance, and compose portfolios are made under conditions of "uncertainty." With uncertainty, assets not only yield income but also, in varying degrees, provide "insurance" against various contingent outcomes. Under uncertainty, where no calculable basis for estimating probabilities exists, history will affect beliefs as to the likelihood of alternatives occurring.

Inasmuch as assets are traded on the basis of their yield under various contingencies and as assets "carry" different proportions of yield and insurance, a rise in the subjective likelihood of events that makes insurance valuable will change the relative prices of assets. The price of the monetary unit is always one, and possession of money assures that units can fulfill contracts denominated in money. A rise in the subjective likelihood that cash to fulfill contracts will not be forthcoming from the production process, therefore, leads to a fall in the price level of assets that are valued for the income they yield relative to the price level of money, current output, and the general level of money wages.

Keynes called the relations that determine the price level of assets "liquidity preference." A rise in liquidity preference, which follows upon systemic failures to meet financial commitments, will lead to a fall in capital asset prices relative to the supply prices of investment output. This, along with the impact of the change in liquidity preference on new financing terms, will decrease investment. Given consumption behavior, a fall in investment activity leads to a fall in income, employment, and profits. In this way Keynes constructed an investment theory of business cycles and a financial theory of investment.

Keynes' theory shunted aside the explanation of employment and income distribution by the forces underlying supply and demand. Upon the appearance of The General Theory, a process of interpretation and reformulation began that led to the incorporation of the underemployment result of Keynes as a special case of the older neoclassical theory. As a result, Keynes' theory was changed from a deep critique of capitalism as an inherently unstable system into a series of banal rules for policy that emphasized the superiority of fiscal interventions over control of the money supply. By the mid-1960's the revolutionary thrust of Keynes' critique of standard economics had been blunted. Only as the capitalist economies began to misbehave in the late 1970's was there a serious attempt by economists to recapture the gist of Keynes' theory.

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